

Report  
of the  
Examination of  
CMG Mortgage Assurance Company  
Madison, Wisconsin  
As of December 31, 2002

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# State of Wisconsin / OFFICE OF THE COMMISSIONER OF INSURANCE

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October 28, 2003

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Commissioners:

In accordance with your instructions, a compliance examination has been made of the  
affairs and financial condition of:

CMG MORTGAGE ASSURANCE COMPANY  
MADISON, WISCONSIN

and this report is respectfully submitted.

## I. INTRODUCTION

The previous examination of the CMG Mortgage Assurance Company (also “the company” or “CMGA”) was conducted in 2001, as of June 30, 2000. The current examination covered the intervening period ending December 31, 2002, and included a review of such 2003 transactions as deemed necessary to complete the examination.

The examination consisted of a review of all major phases of the company's operations, and included the following areas:

- History
- Management and Control
- Corporate Records
- Conflict of Interest
- Fidelity Bonds and Other Insurance
- Employees' Welfare and Pension Plans
- Territory and Plan of Operations
- Affiliated Companies
- Growth of Company
- Reinsurance
- Financial Statements
- Accounts and Records
- Data Processing

Emphasis was placed on the audit of those areas of the company's operations accorded a high priority by the examiner-in-charge when planning the examination. Special attention was given to the action taken by the company to satisfy the recommendations and comments made in the previous examination report.

The section of this report titled "Summary of Examination Results" contains comments and elaboration on those areas where adverse findings were noted or where unusual situations existed. Comments on the remaining areas of the company's operations are contained in the examination work papers.

The company is annually audited by an independent public accounting firm as prescribed by s. Ins 50.05, Wis. Adm. Code. An integral part of this compliance examination was the review of the independent accountant's work papers. Based on the results of the review of these work papers, alternative or additional examination steps deemed necessary for the completion of this examination were performed. The examination work papers contain documentation with respect to the alternative or additional examination steps performed during the course of the examination.

## **II. HISTORY AND PLAN OF OPERATION**

CMG Mortgage Assurance Company was originally incorporated on March 4, 1969, under the name Investors Mortgage Insurance Company of California, organized as a mortgage guaranty insurer domiciled in the State of California. The company was initially established as a subsidiary of Investors Mortgage Insurance Company ("IMIC"), and wrote mortgage guaranty insurance policies on first mortgages in California. In 1974, IMIC obtained mortgage guaranty insurance authority in California, and the company subsequently ceased writing new business and reinsured all of its then existing insurance risks with IMIC.

The company's articles of incorporation were amended on September 23, 1980, changing the name of the company to Investors Equity Insurance Company, Inc. ("IEIC"), and changing its line of business authorization from mortgage guaranty insurance to credit insurance. The company remained a dormant corporation through May 12, 1981, at which time it obtained license authority and commenced writing mortgage guaranty insurance on second mortgages.

Ownership of 100% of the capital stock of IEIC was acquired by Investors Mortgage Insurance Holding Company ("IMIHC") effective December 31, 1981, when the company's parent merged into IMIHC. IEIC continued writing new business through 1986, at which time it again suspended issuance of new insurance policies. Effective April 14, 1994, CUNA Mutual Investment Corporation ("CMIC"), a subsidiary of CUNA Mutual Insurance Society ("CMIS"), acquired all of the capital stock of IMIHC, and thereby indirectly acquired control of the company. On June 1, 1994, IMIHC paid to CMIC an extraordinary dividend consisting of 100% of the capital stock of the company. In 1999, the name of the company was changed to CMG Mortgage Assurance Company, the name presently used by the company. CMGA redomiciled from California to Wisconsin effective June 1, 2000, as a mortgage guaranty insurer.

Effective October 1, 2000, PMI Insurance Company ("PMI"), a subsidiary of The PMI Group, Inc. ("TPG"), purchased 50% of the capital stock of CMGA from CMIC, and CMGA became a jointly owned subsidiary of CMIC and PMI. CMIC and PMI entered into a contractual joint venture to own and operate CMGA as a direct insurer to write insurance coverages on junior lien second-mortgage loans originated by credit unions.

CMIC and PMI each own a 50% interest in the capital stock of each of the three CMG mortgage guaranty insurers, including CMGA, CMG Mortgage Reinsurance Company ("CMG Re"), and CMG Mortgage Insurance Company ("CMG"). The joint venture was initially formed in 1994 for joint ownership and operation of CMG. The objective of the CMG joint venture between CMIC and PMI was to establish a strategic alliance to offer mortgage guaranty insurance products and services to credit unions that originate residential mortgage loans. The strategic alliance was undertaken to combine and employ the expertise of the two parent organizations, with PMI contributing its specialized knowledge and business systems for mortgage guaranty insurance operations, and with CMIC having close business associations with and specialized knowledge of the credit union industry. The CMG mortgage insurance companies do not have their own employees, and their operating functions are provided by affiliated companies within the two parent holding company organizations, pursuant to numerous affiliated services agreements. Further discussion of affiliated relationships and affiliated services agreements is included in the section of this report captioned "Affiliated Companies."

The company's main administrative offices are currently located in San Francisco, California, where the company shares office space with CMG and CMG Re, to facilitate the sharing and allocation of resources. CMGA conducts policy administration, actuarial, marketing, and underwriting operations in conjunction with those operations conducted on behalf of CMG Mortgage Insurance Company.

The business plan of CMGA is to operate as a direct insurer of mortgage guaranty policies covering default risks on junior lien second mortgage loans originated by credit unions. The company is licensed in 44 states and in the District of Columbia, and has a license application pending in Alabama. The company began writing second lien mortgage business in the third quarter of 2001. The following table is a summary of premiums written by the company in 2002. The growth of the company is discussed in the section of this report captioned "Financial Data."

<b>Line of Business</b>	<b>Direct Premium</b>	<b>Reinsurance Assumed</b>	<b>Reinsurance Ceded</b>	<b>Net Premium</b>
Mortgage guaranty	<u>\$50,639</u>	<u>\$0</u>	<u>\$0</u>	<u>\$50,639</u>
Total All Lines	<u>\$50,639</u>	<u>\$0</u>	<u>\$0</u>	<u>\$50,639</u>

### III. MANAGEMENT AND CONTROL

#### Board of Directors

The board of directors consists of eight members. Directors are elected annually to serve a one-year term. Officers are elected at the board's annual meeting.

Each member of the CMGA board of directors is a senior executive in one of the two immediate parent companies, CMIC and PMI, and may also serve as an executive or a director of one or more additional companies within the respective holding companies. CMIC and PMI each have the right to designate the same number of directors to the board of CMGA, and to vote their respective shares in favor of their respective designees. As provided in the CMG, CMG Re, and CMGA Shareholders Agreements, each director of CMG also serves as a director of CMG Re and of CMGA, and the boards of directors of the three CMG mortgage guaranty insurers have common membership. The board members currently receive no compensation for serving on the board.

Currently, the board of directors consists of the following persons:

<b>Name and Residence</b>	<b>Principal Occupation</b>	<b>Term Expires</b>
Walter E. Campion Danville, CA	Sr. VP, Claims & Loss Mitigation PMI Group	2003
James R. McCourt Sun Prairie, WI	Sr. VP, Claims & Loss Mitigation CUNA Mutual Group	2003
Daniel E. Meylink, Sr. Middleton, WI	Chief Officer, Lending Solutions Group CUNA Mutual Group	2003
Peter Pannes San Anselmo, CA	Sr. Vice President & General Manager CMG Mortgage Insurance Company	2003
Faye A. Patzner Middleton, WI	Chief Legal Officer CUNA Mutual Group	2003
Kathleen R. Schroeder Novato, CA	Sr. Vice President & General Manager CMG Mortgage Insurance Company	2003
Arthur P. Slepian San Francisco, CA	Senior Vice President PMI Capital Corp	2003
Stephen L. Smith Alamo, CA	President & COO PMI Mortgage Insurance Company	2003



## Officers of the Company

The officers of CMG Mortgage Assurance Company are appointed by the directors at the annual meeting of the CMGA board of directors, to serve a one-year term.

Each officer of CMGA is an officer in one of the two immediate parent companies, CMIC and PMI, and may also serve as an officer of one or more additional companies within the respective holding companies. Each officer of CMGA also holds the corresponding office in CMG and in CMG Re, and the three CMG mortgage guaranty insurers have a shared corps of executive officers.

As provided in the CMG, CMG Re, and CMGA Shareholders Agreements, the chairman of the board of directors of CMG also serves as the chairman of the boards of CMG Re and CMGA. The shared board chairmanship of CMG, CMG Re, and CMGA rotates annually between CMIC and PMI designees, and the president of the boards of directors of the CMG mortgage insurance companies shall be a person designated by CMIC.

CMGA officers appointed by the board of directors and serving at the time of this examination are as follows:

<b>Name</b>	<b>Office</b>	<b>2002 Compensation</b>
L. Stephen Smith	Chairman of the board	*
Daniel E. Meylink, Sr.	Vice Chairman	*
Michael B. Kitchen	President	*
Donald P. Lofe, Jr.	Treasurer	*
Earl W. Sealy	Secretary	*
James McCourt	Vice President	\$304,876
Peter C. Pannes	Senior Vice President & General Manager	126,149
Kathleen Schroeder	Senior Vice President & General Manager	*
Michael Warner	Vice President – Underwriting & Operations	269,792
Pamela G. Black	Vice President – Information Technology	165,972
Brian Shepherd	Vice President – Sales	179,500

\*The executive compensation numbers include the amounts reported on the National Association of Insurance Commissioners (NAIC) Supplemental Compensation Exhibit filed with this office.

The above individuals' 2002 compensation was not reported. This is further discussed in the section of this report captioned "Summary of Current Examination Results."

### **Committees of the Board**

The company's bylaws provide for the formation of one or more standing committees or other committees of the board, to be appointed by the board of directors. The company currently has one standing committee of the board of directors, having the following membership.

#### **Audit Committee**

James McCourt, Chair  
Arthur Slepian

The Audit Committee is comprised of two members chosen by the board of directors, with equal representation by each of the two joint venture shareholders of CMG. The Audit Committee reviews financial information, systems of internal controls, and the audit process in order to assist the board in its oversight of the company.

### **Executive Committees Other Than Committees of the Board**

CMG bylaws provide that management of company operations shall be conducted by a management committee composed of two to six committee members appointed by the CMG board of directors. The Management Committee functions as a board-appointed executive body that, subject to the overriding authority of the board of directors, has authority to act on all matters related to the day-to-day operation of the company, so long as such actions are authorized by the board-approved annual business plan and provided that such actions are not specifically reserved to the board of directors. The Management Committee shall act by the affirmative majority of its members, except that the committee shall act by the unanimous vote of all its members with regard to specific matters of business as enumerated in the bylaws.

Members of the Management Committee need not be members of the board of directors. Historically, the practice of the CMG board has been to appoint two CMG directors, with equal representation by each of the two joint venture shareholders of CMG. The bylaws of CMG Re and CMGA also provide for respective board appointment of a Management Committee executive body, and the Management Committees of CMG, CMG Re, and CMGA have common membership. The CMG Management Committee currently has the following membership:

**Management Committee**  
Peter Pannes  
Kathleen Schroeder

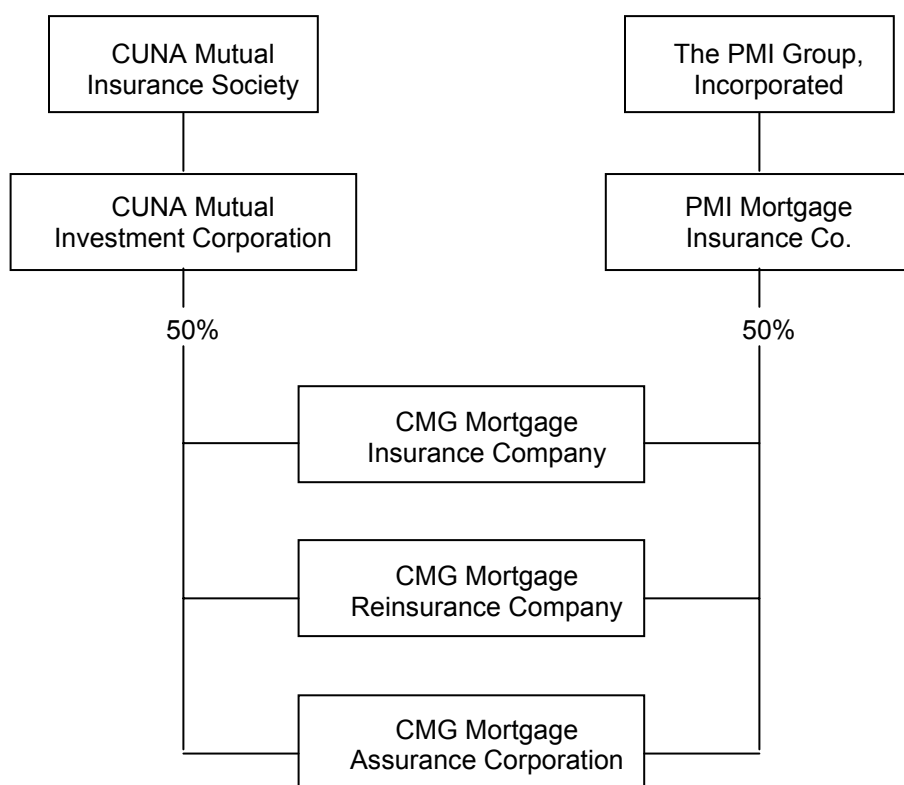
#### **IV. AFFILIATED COMPANIES**

CMG Mortgage Assurance Company is a joint venture enterprise, and is a member of two independent holding company systems. The company is jointly owned and controlled by CUNA Mutual Investment Corporation (CMIC) and PMI Mortgage Insurance Co. (PMI), which are in turn wholly owned subsidiaries in the CUNA Mutual Insurance Society (CMIS) and The PMI Group, Inc. (TPG), holding company systems, respectively. CUNA Mutual Insurance Society is a mutual life insurance company domiciled in Wisconsin, and is the holding company parent for the CUNA Mutual Group. The PMI Group, Inc., a corporation domiciled in Delaware and publicly traded on the New York Stock Exchange, is an insurance holding company.

CMIC and PMI each own 50% of the capital stock of CMG, CMG Re, and CMGA, and collectively hold 100% of the equity ownership of each company. CMG's management and operations are conducted pursuant to a joint venture strategic alliance of CMIC and PMI, established by the CMG Shareholders Agreement effective September 8, 1994, by the CMG Re Shareholders Agreement effective May 27, 1999, and by the CMGA Shareholders Agreement effective October 1, 2000. All of the business operation functions of the CMG mortgage guaranty insurers, including personnel, legal and administrative services, premium billing and receipt, policy issuance and administration, claims processing and adjudication, asset management and investment, and general accounting and financial reporting operations, are provided to the companies by affiliates from within the CMIS and PMI holding companies, through the provisions of various affiliated services agreements.

The following organizational chart depicts the holding company relationships among the significant affiliates of the company. A brief description of the significant affiliates of CMGA follows the organizational chart, which is followed by a summary of the service agreement relationships between the company and its affiliates.

**Organizational Chart  
As of December 31, 2002**



**CUNA Mutual Insurance Society (CMIS)**

CUNA Mutual Insurance Society and its affiliates provide group and individual life insurance products, accident and health insurance products, and other financial products and services to credit unions, credit union service organizations, and credit union members. CMIS business activities are conducted in all states, the District of Columbia, and in countries and political jurisdictions throughout the world.

As of December 31, 2002, CMIS's audited financial statements reported total admitted assets of \$2.6 billion, total liabilities of \$2.1 billion and policyholders' capital and surplus of \$500 million. Operations for 2002 produced net income of \$8.4 million on revenues of \$1.5 billion.

### **CUNA Mutual Investment Corporation (CMIC)**

CUNA Mutual Investment Corporation is the holding company for United States based companies in the CUNA Mutual Group. The subsidiaries held by CMIC include 100% ownership of Members Life Insurance Company (a Wisconsin life and health insurer) and CUMIS Insurance Society, Inc. (a Wisconsin property and casualty insurer), 100% ownership of insurance agencies that support the activities of the CUNA Mutual Group, and 50% ownership in each of the three insurers in the CMG Mortgage Insurance Group.

As of December 31, 2002, CMIC's unaudited financial statements reported total assets of \$514 million, total liabilities of \$40 million, and total stockholders' equity of \$474 million. Operations for 2002 produced a net loss of \$20 million after distributing the equity share of affiliated earnings and taxes.

### **The PMI Group, Inc. (TPG)**

The PMI Group, Inc., is an insurance holding company organized in December 1993 pursuant to the laws of the State of Delaware. TPG was originally a wholly owned subsidiary of Allstate Insurance Company (Allstate), an insurance subsidiary of The Allstate Corporation. In an April 18, 1995, initial public offering, Allstate sold 36.75 million shares of TPG common stock, representing 70% ownership interest of TPG. Subsequent to the 1995 public offering of TPG, Allstate divested all of its remaining 30% ownership interest in TPG through an exchange of 12.9 million shares of TPG common stock to redeem outstanding Allstate exchangeable notes, and through the sale of 2.8 million shares of TPG common stock that remained in Allstate ownership following the Allstate exchange note redemptions.

Through its subsidiary PMI, TPG provides private mortgage insurance to mortgage lenders in the United States. Other TPG subsidiaries provide mortgage guaranty reinsurance, private mortgage insurance in Australia and New Zealand, home finance industry risk management products and services, and title insurance.

As of December 31, 2002, TPG's audited financial statements reported total assets of \$3.5 billion, total liabilities of \$1.3 billion, and shareholders' equity of \$2.2 billion. Operations for 2002 produced net income of \$346 million on revenues of \$1.1 billion.

**PMI Mortgage Insurance Co. (PMI)**

PMI Mortgage Insurance Co., was incorporated November 10, 1972, as an Arizona stock mortgage guaranty insurance company. From 1973 until 1994, PMI was a wholly owned subsidiary of Allstate Insurance Company. Effective November 28, 1994, Allstate contributed all of the outstanding capital stock of PMI to TPG.

PMI writes residential mortgage guaranty insurance, providing primary insurance coverage on first lien mortgage loans and, beginning in 1997, providing a government sponsored mortgage pool insurance product that is used as an element of credit enhancement for secondary market mortgage loan securities transactions. PMI is licensed to engage in mortgage guaranty insurance in all fifty states and in the District of Columbia.

As of December 31, 2002, PMI's audited statutory financial statements reported total admitted assets of \$2.7 billion, total liabilities of \$2.4 billion, and policyholders' capital and surplus of \$267 million. Operations for 2002 produced net income of \$353 million on premium revenues of \$550 million.

**CMG Mortgage Reinsurance Company (CMG Re)**

CMG Mortgage Reinsurance Company was incorporated May 27, 1999, as a jointly owned subsidiary of CMIC and PMI. CMG Re is authorized as a mortgage guaranty insurer, licensed solely in the State of Wisconsin. CMIC and PMI each contributed initial capital of \$1.5 million to CMG Re in 1999, and CMG Re commenced business August 26, 1999. CMG Re was established to assume from CMG Mortgage Insurance Company mortgage loan reinsurance coverages of up to 25% of individual mortgage loans written on a direct basis by CMG, the CMG Re coverages being excess of coverages for up to 25% of each insured mortgage loan that are retained by CMG.

As of December 31, 2002, CMG Re's audited statutory financial statements reported total admitted assets of \$8.1 million, total liabilities of \$4.1 million, and policyholders' capital and surplus of \$4.0 million. Operations for 2002 produced net income of \$326 thousand on revenues of \$2.7 million.

**CMG Mortgage Insurance Company (CMG)**

CMG Mortgage Insurance Company was originally incorporated in 1980 as an Illinois domiciled mortgage guaranty insurer. On April 14, 1994, CUNA Mutual Investment Corporation purchased 100% of the capital stock of CMG. On June 23, 1994, PMI purchased from CMIC 45% of the issued and outstanding stock of CMG, and on September 8, 1994, CMIC and PMI executed the CMG Shareholders Agreement that established a contractual joint venture arrangement and joint management of CMG under a strategic alliance of CMIC and PMI.

CMG resumed writing new business in 1994, and redomiciled to Wisconsin effective November 30, 1994. PMI's ownership interest in CMG increased to 50% in 1998 through PMI's purchase of 200,000 additional shares of CMG capital stock, and presently CMIC and PMI each hold equal 50% ownership interests in the capital stock of CMG. CMG is licensed in all 50 states and the District of Columbia, and issues mortgage guaranty insurance policies on first-lien residential mortgage loans originated by credit unions.

As of December 31, 2002, CMG's audited statutory financial statements reported total admitted assets of \$184 million, total liabilities of \$103 million, and policyholders' capital and surplus of \$81 million. Operations for 2002 produced net income of \$11 million on revenues of \$40 million.

**Affiliated Agreements**

As previously described, each of the three CMG mortgage guaranty insurers is organized as a joint venture enterprise by CMIC and PMI, with each parent organization having responsibility for specified portions of the operations and management of CMG, CMG Re, and CMGA. The rights and responsibilities of affiliates who participate in the joint venture are formalized in agreements between CMIC and PMI (and their affiliates) and each respective CMG mortgage insurance company. Affiliated agreements that pertain to CMGA are summarized below. Each CMGA affiliated agreement became effective October 1, 2000, concurrent with the adoption of the CMGA Shareholders Agreement.



## **PMI Services Agreement**

Pursuant to the PMI Services Agreement, PMI provides the following services:

1. General Management—management assistance in accordance with the Shareholders Agreement, including but not limited to services of specified management personnel,
2. Actuarial Services,
3. Accounting Services,
4. Federal Income Tax Return,
5. Legal and Government Relations,
6. Special Reports.

In compensation to PMI for services provided, CMGA pays to PMI a quarterly service fee based on actual cost of services. The agreement includes detailed performance standards for PMI services. The agreement is continuous until the termination of the CMGA Shareholders Agreement. CMGA or PMI may terminate the agreement if the other party is in material default for 60 days following notice of default.

## **CMIC Services Agreement**

Pursuant to the CMIC Services Agreement, CMIC provides the following services:

1. General Management—management assistance in accordance with the Shareholders Agreement, including but not limited to services of specified management personnel,
2. Purchase of insurance coverages, including coverages for directors, officers and employees,
3. Investment Accounting Services,
4. Legal and Government Relations, including those generally related to maintenance of insurance licenses, agent and agency licensing, corporate transactions, and general corporate governance,
5. Facilities Management / Administration, and
6. Special Reports.

In compensation to CMIC for services provided, CMGA pays to CMIC a quarterly service fee based on actual cost of services. The agreement includes detailed performance standards for CMIC services. The agreement is continuous until the termination of the CMGA Shareholders Agreement. CMGA or CMIC may terminate the agreement if the other party is in material default for 60 days following notice of default.

### **Members Capital Advisors, Inc. Investment Advisory Agreement**

Pursuant to the Investment Advisory Agreement, CMGA appointed Members Capital Advisors, Inc. ("MCA"), to act as CMGA's sole investment advisor and investment portfolio manager. MCA, a duly licensed registered investment advisor domiciled in the State of Iowa, is 50% owned by CMIC and 50% owned by CUNA Mutual Life Insurance Company ("CMLIC"), an Iowa domiciled life insurer. CMIS and its affiliates and CMLIC are affiliated through common management and by virtue of an Agreement of Permanent Affiliation effective July 1, 1990.

Specific services provided to CMGA by MCA are the following:

1. Makes investment decisions and is responsible for investment and reinvestment of the CMGA investment securities portfolio,
2. Performs research, statistical analysis and continuous supervision of the CMGA portfolio,
3. Provides to CMGA and its agent the information required to prepare and file all necessary statutory statements, tax returns, and any other reports or returns of a regulatory nature;
4. Monitors systems and procedures for proper functioning of all investment activities to ensure compliance with the requirements of applicable federal and state laws, rules, and regulations,
5. Renders any periodic and special reports reasonably requested.

In compensation to MCA for services provided, CMGA pays to MCA a monthly service fee based on a fractional percentage of the end-of-month value of securities and cash managed by the advisor. The agreement is continuous until termination of the CMIC Services Agreement between CMGA and CMIC. CMGA or MCA may terminate the agreement in the event of the default of the other party. If MCA fails to meet the performance standards of the contract, the contract may be terminated by 30 days written notice to MCA given either by CMGA or by CMIC.

**Trade Name License Agreement**

Pursuant to the Trade Name License Agreement, CMIS granted to CMGA a royalty-free, non-exclusive right and license in the United States to use the term "CMG," a CUNA Mutual Group trade name, as part of CMGA's corporate name, corporate trade name, and corporate trademarks and service marks. The agreement establishes requirements and prohibitions on CMGA's authority to use the term "CMG." The agreement provides that any use of the mark by CMGA shall inure for the benefit of CUNA Mutual Group, and provides that the company acknowledges the validity of the mark "CMG" and CUNA Mutual Group's exclusive right, title, and interest in the mark. So long as CMGA shall make regular commercial use of the authorized trademark, the agreement is continuous until the termination of the CMGA Shareholders Agreement or upon CMGA's violation of the contract provisions for CUNA's exclusive rights under the contract, CMGA's assignment of the contract, or CMGA's improper use of the trademark. CMGA may terminate the contract upon 30 days written notice.

**Software License Agreement**

Pursuant to the Software License Agreement, PMI granted to CMGA a non-exclusive right to use specified, agreed upon items of computer software that PMI or any member of the PMI Group has the right to license. The contracted software is used by members of the PMI group to perform underwriting or other services, for which PMI either has all right, title and interest or has the right to license. The agreement provides that use of the software shall be limited to CMGA, that the software will be used solely for the processing of CMGA's own business which is originated in the credit union system, that CMGA shall not modify, adapt, translate, disassemble, decompile, reverse engineer or attempt to derive source code for the software, and that the company shall not make the software available to PMI competitors. CMGA may terminate the agreement upon written notice to PMI. PMI may terminate the agreement in the event that CMGA or CUNA violates any material provision of the agreement, if CMGA ceases operations, or if CMGA fails to use the software for any 180-day period.

## **CMG Services Agreement with CMGA**

Pursuant to the CMG Services Agreement with CMGA, CMG provides to CMGA various policy administration services pertaining to the insurance policies written and issued by CMGA. Services provided by CMG under the agreement include the following:

1. Issue CMGA certificates of insurance for new business and bill insured for initial premium due,
2. Send renewal notices to CMGA insureds,
3. Collect all CMGA renewal premium checks and supporting materials mailed by insureds, remitting checks to CMGA, and directing CMGA to return to insureds any overpayments, mistaken payments and refunds due to cancellations. CMGA premium collected by CMG is held by CMG as a fiduciary for CMGA,
4. Monitor defaults, mitigate losses utilizing mitigation practices and philosophy in effect, review claims for fraud indicators prior to CMGA payment, and direct CMGA to pay claims,
5. Supply CMGA with monthly reports, including reports of policyholder count showing loans in default and loans current, and claims paid during the month and inception-to-date, and
6. Supply CMGA with all information necessary for preparation of periodic financial statements and for the payment of premium taxes.

In compensation to CMG for services provided, CMGA pays to CMG a quarterly service fee based on actual cost of services. The agreement provides that the performance standards for CMG services shall be that of best efforts and the exercise of the highest degree of professional competence. The agreement may be terminated by either party providing 60 days written notice. Either party may terminate the agreement at any time if the other party is in default for 60 days following written notice of default.

## **V. REINSURANCE**

The company does not cede or assume insurance risks, and is not party to any reinsurance treaties.

## **VI. FINANCIAL DATA**

The following financial statements reflect the financial condition of the company as reported in the December 31, 2002, annual statement to the Commissioner of Insurance. Also included in this section are schedules that reflect the growth of the company, NAIC Insurance Regulatory Information System (IRIS) ratio results for the period under examination, and the compulsory and security surplus calculation. Adjustments made as a result of the examination are noted at the end of this section in the area captioned "Reconciliation of Surplus per Examination."

**CMG Mortgage Assurance Company**  
**Assets**  
**As of December 31, 2002**

	<b>Assets</b>	<b>Nonadmitted Assets</b>	<b>Net Admitted Assets</b>
Bonds	\$8,577,316	\$ 0	\$8,577,316
Cash	12,194		12,194
Short-term investments	447,671		447,671
Federal and foreign income tax recoverable and interest thereon	258,407	92,069	166,338
Electronic data processing equipment and software	6,216		6,216
Interest, dividends, and real estate income due and accrued	<u>141,517</u>	<u>          </u>	<u>141,517</u>
Total Assets	<u>\$9,443,321</u>	<u>\$92,069</u>	<u>\$9,351,252</u>

**CMG Mortgage Assurance Company**  
**Liabilities, Surplus, and Other Funds**  
**As of December 31, 2002**

Losses	\$	4,000	
Loss adjustment expenses		1,000	
Other expenses (excluding taxes, licenses, and fees)		13,000	
Taxes, licenses, and fees (excluding federal and foreign income taxes)		10	
Federal and foreign income taxes		(30,049)	
Unearned premiums		7,001	
Payable to parent, subsidiaries, and affiliates		1,027,981	
Payable for securities		1,125	
Write-ins for liabilities:			
Contingency reserve		73,921	
Premium paid in advance		<u>2,069</u>	
Total Liabilities			\$1,100,058
Common capital stock		2,000,000	
Gross paid in and contributed surplus		3,759,998	
Unassigned funds (surplus)		<u>2,491,196</u>	
Surplus as Regards Policyholders			<u>8,251,194</u>
Total Liabilities and Surplus			<u>\$9,351,252</u>



**CMG Mortgage Assurance Company**  
**Summary of Operations**  
**For the Year 2002**

**Underwriting Income**

Premiums earned		\$ 46,349
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Deductions:

Losses incurred	\$4,000	
Loss expenses incurred	1,000	
Other underwriting expenses incurred	525,636	
Write-ins for underwriting deductions:		
Increase in contingency reserve	23,175	
Withdrawal of the 1992 contingency reserve	<u>(39,000)</u>	
Total underwriting deductions		<u>514,811</u>
Net underwriting gain or (loss)		(468,462)

**Investment Income**

Net investment income earned	444,626	
Net realized capital gains or (losses)	<u>5,805</u>	
Net investment gain or (loss)		<u>450,431</u>

Net Loss		<u>\$(18,031)</u>
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**CMG Mortgage Assurance Company**  
**Cash Flow**  
**As of December 31, 2002**

Premiums collected net of reinsurance	\$ 50,639	
Deduct:		
Underwriting expenses paid	<u>525,626</u>	
Cash from underwriting		\$(474,987)
Net investment income		431,629
Net cash from operations		\$ (43,358)
Proceeds from investments sold, matured, or repaid:		
Bonds	<u>1,185,147</u>	
Total investment proceeds		1,185,147
Cost of investments acquired (long-term only):		
Bonds	2,238,443	
Miscellaneous applications	<u>282</u>	
Total investments acquired		<u>2,238,725</u>
Net cash from investments		(1,053,578)
Cash provided from financing and miscellaneous sources:		
Net transfers from affiliates	534,189	
Other cash provided	<u>3,369</u>	
Total		537,558
Net cash from financing and miscellaneous sources		<u>537,558</u>
Net change in cash and short-term investments		(559,378)
<b>Reconciliation</b>		
Cash and short-term investments,		
December 31, 2001		<u>1,019,243</u>
Cash and short-term investments,		
December 31, 2002		<u>\$ 459,865</u>

**CMG Mortgage Assurance Company  
Policyholders' Position Calculation  
As of December 31, 2002**

Surplus as regards policyholders	\$8,251,194	
Contingency reserve	<u>73,921</u>	
Total policyholders position		\$8,325,115
Net minimum policyholders' position:		
Junior Liens—Individual loans:		
Loan-to-value more than 75%	\$425,688	
Loan-to-value 50 - 75%	11,549	
Loan-to-value less than 50%	<u>30,671</u>	
Total individual loans	<u>467,908</u>	
Total minimum policyholder position		<u>467,908</u>
Excess of total policyholders' position over minimum policyholders' position		<u>\$7,857,207</u>

**CMG Mortgage Assurance Company  
Reconciliation and Analysis of Surplus  
For the Three-Year Period Ending December 31, 2002**

The following schedule is a reconciliation of total surplus during the period under examination as reported by the company in its filed annual statements:

	<b>2002</b>	<b>2001</b>	<b>2000</b>
Surplus, beginning of year	\$8,102,886	\$8,057,736	\$6,673,544
Net income	(18,031)	45,150	184,192
Change in net deferred income tax	258,407		
Change in non-admitted assets	(92,069)		
Capital changes:			
Paid in			1,200,000
Surplus, end of year	<u>\$8,251,194</u>	<u>\$8,102,886</u>	<u>\$8,057,736</u>

**CMG Mortgage Assurance Company  
Insurance Regulatory Information System  
For the Three-Year Period Ending December 31, 2002**

The following is a summary of NAIC Insurance Regulatory Information System (IRIS) results for the period under examination. Exceptional ratios are denoted with asterisks. A discussion of the exceptional ratios may be found after the IRIS ratios

	<b>Ratio</b>	<b>2002</b>	<b>2001</b>	<b>2000</b>
#1	Gross Premium to Surplus	1.0%	0.0%	0.0%
#2	Net Premium to Surplus	1.0	0.0	0.0
#3	Change in Net Writings	963.0*	999.0*	-99.0*
#4	Surplus Aid to Surplus	0.0	0.0	0.0
#5	Two-Year Overall Operating Ratio	-99.0	0.0	0.0
#6	Investment Yield	5.1	5.7	5.6
#7	Change in Surplus	2.0	1.0	21.0
#8	Liabilities to Liquid Assets	12.0	7.0	2.0
#9	Agents' Balances to Surplus	0.0	0.0	0.0
#10	One-Year Reserve Devel. to Surplus	0.0	0.0	0.0
#11	Two-Year Reserve Devel. to Surplus	0.0	0.0	0.0
#12	Estimated Current Reserve Def. To Surplus	0.0	0.0	0.0

IRIS ratio No. 3, Change in Net Writings, reflects the increase or decrease in net premium written reported as a percentage of net premium written in the prior year. Exceptional results for the years are due to the company being in run-off and then in the third quarter of 2001 starting to write new business.

### Growth of CMG Mortgage Assurance Company

Year	Admitted Assets	Liabilities	Surplus As Regards Policyholders	Net Income
2002	\$9,351,252	\$1,100,058	\$8,251,194	\$(18,031)
2001	8,673,894	571,008	8,102,887	45,150
2000	8,203,452	145,716	8,057,736	184,192

Year	Gross Premium Written	Net Premium Written	Premium Earned	Loss And LAE Ratio	Expense Ratio	Combined Ratio
2002	\$50,639	\$50,639	\$46,349	10.8%	-8,230.7%	-8,219.9%
2001	4,764	4,764	2,054	10.8	1,006.8	1,017.5
2000	0	0	7	0.0	9,237.5	9,237.5

CMG Mortgage Assurance was running off its existing business in the beginning of the examination period. Starting in 2001, the company began writing direct business on second liens. The company's loss ratio for this business has been consistent for 2001 and 2002. To date, this business has not been profitable; however, the company's investment income has offset the majority underwriting losses in these years.

**Reconciliation of Surplus per Examination**

The current examination did not make any reclassification of account balances or adjustment to surplus as reported by the company at December 31, 2002.

## **VII. SUMMARY OF EXAMINATION RESULTS**

### **Compliance with Prior Examination Report Recommendations**

There was one specific comments and recommendations in the previous examination report. Comments and recommendations contained in the last examination report and actions taken by the company are as follows:

1. Affiliated Agreements—It is recommended that the company comply with the terms of its intercompany agreements or amend such agreements to reflect the actual practice for provision of services and allocation of costs, and that the company ensure that all of its agreements with affiliates are maintained so as to reflect the substance of all transactions and allocations between respective contracting parties.

Action—Compliance

## **Summary of Current Examination Results**

### **Biographical Reports**

Pursuant to s. Ins 6.52, Wis. Adm. Code, the biographical data relating to company officers and directors should be filed with this office within 15 days after such appointment or election. One director's biographical report was not filed within this time frame. During fieldwork, the company provided a biographical report for this director; however, the report did not include all the information by s. Ins 6.52, Wis. Adm. Code. It is recommended that the company file biographical reports of its directors within 15 days of election and that the biographical report include the information outlined in form B of s. Ins 6.52, Wis. Adm. Code.

### **Executive Compensation**

A review of the Wisconsin Report on Executive Compensation (Form 22-060) for 2002 noted the company is not completing this form, but is completing the NAIC Supplemental Compensation Exhibit in place of the Wisconsin Report on Executive Compensation annual supplement. It is noted that the directions for the NAIC Supplemental Exhibit and those for the Wisconsin Report of Executive Compensation vary slightly and the company should be reporting compensation to this office on the Wisconsin form. The executive compensation form included the chief executive officer, however, it was noted this was not an appointed officer position in the section of this report captioned "Management and Control." Testing also disclosed that the company should have reported the president due to the fact that his salary exceeded the threshold for reporting. In addition, an amount reported for one of the officers did not reconcile to the detail provided. For officers that are PMI employees, the amounts reported on the form excluded the amounts for executive stock options. It is recommended that the company complete the Wisconsin Report on Executive Compensation (Form 22-060) in accordance with its instructions.

### **Remittances and Items not Allocated**

Examination review of the write-in liability titled "Premiums paid in Advance" found that this balance consists of premiums in suspense. Pursuant to the NAIC Annual Statement Instructions – Property and Casualty these amounts should be reported in the line item Remittances and Items not Allocated. Due to the immaterial nature of the balance no



reclassification was made. It is recommended that the company report its suspense premiums as Remittances and Items not Allocated pursuant to the NAIC Annual Statement Instructions – Property and Casualty.

#### **Affiliated Transactions**

Examination review of the payable to CMG indicated that the amount reported in the annual statement was different than the receivable on CMG's annual statement. In addition, this balance was settled in March, 2003. Pursuant to the services agreement, intercompany balances should be settled within 30 days after the end of each quarter. Therefore, this balance should have been settled in January since it included amounts for October, November, and December. It is recommended that the company settle intercompany balances in accordance with the affiliated contracts and ensure that amounts reported by the various affiliates reconcile correctly.

## **VIII. CONCLUSION**

CMG Mortgage Assurance Company's financial statements as of December 31, 2002 reported total admitted assets of \$9,351,252, total liabilities of \$1,100,058, and policyholders' capital and surplus of \$8,251,194. No reclassifications or adjustments were made to surplus as a result of the examination.

Effective October 1, 2000, PMI purchased from CMIC 50% of the capital stock of CMGA, and CMGA became a jointly owned subsidiary of CMIC and PMI. CMIC and PMI also each own 50% equity interest in CMG Mortgage Insurance Company and CMG Mortgage Reinsurance Company. CMG, CMG Re, and CMGA, the three insurers that comprise the CMG mortgage insurance group, are each managed and operated by CMIC and PMI as a joint venture enterprise, pursuant to respective Shareholder Agreements established for each of the three insurers in the group. A strategic alliance of CMIC and PMI, the group exists to provide mortgage guaranty products and services to credit unions who originate residential mortgage loans. The joint venture ownership of CMGA was established to provide insurance coverages on junior lien second-mortgage loans that are issued by credit unions to their credit union members.

CMGA ceased writing new business in 1986, and its existing book of business is in run-off. In the third quarter of 2001, the company began writing the risks on second lien mortgage business.

The company complied with the prior examination recommendation. The current examination resulted in four recommendations as summarized on the following page.

## IX. SUMMARY OF COMMENTS AND RECOMMENDATIONS

1. Page 30 - Biographical Reports—It is recommended that the company file biographical reports of its directors within 15 days of election and that the biographical report include the information outlined in form B of s. Ins 6.52, Wis. Adm. Code.
2. Page 30 - Executive Compensation—It is recommended that the company complete the Wisconsin Report on Executive Compensation (Form 22-060) in accordance with its instructions.
3. Page 31 - Remittances and Items not Allocated—It is recommended that the company report its suspense premiums as Remittances and Items not Allocated pursuant to the NAIC Annual Statement Instructions – Property and Casualty.
4. Page 31 - Affiliated Transactions—It is recommended that the company settle intercompany balances in accordance with the affiliated contracts and ensure that amounts reported by the various affiliates reconcile correctly.

## **X. ACKNOWLEDGMENT**

The courtesy and cooperation extended during the course of the examination by the officers and employees of the company are acknowledged.

In addition to the undersigned, the following representatives of the Office of the Commissioner of Insurance, State of Wisconsin, participated in the examination:

<b>Name</b>	<b>Title</b>
Ryan Hanson	Insurance Financial Examiner
Amy Wolff	Insurance Financial Examiner
Randy Milquet	Insurance Financial Examiner—Advanced

Respectfully submitted,

Danielle C. Rogacki  
Examiner-in-Charge